

THE WHITE HOUSE

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DECISION MEMORANDUM FOR THE CABINET

FROM:

ROBERT CARLESON, EXECUTIVE SECRETARY,
HUMAN RESOURCES CABINET COUNCIL

SUBJECT:

Tuition Tax Credits

SUMMARY

The Working Group on Tuition Tax Credits of the Cabinet Council on Human Resources has reviewed alternative ways to fulfill the President's commitment to enact a tuition tax credit bill in the 97th Congress.

A proposed draft Administration bill, "The Educational Opportunity and Equity Act of 1982", has been developed and forwarded by the Working Group. The major elements of the bill include:

- **Tax Equity:** The purpose of the Act is to provide tax relief to parents who bear the double burden of public and private school costs.
- **Limited Coverage:** The credit is restricted to parents of children in private, non-profit, elementary or secondary schools.
- **A Phase-In of Credits:** The policy decisions are the subject of this meeting; a decision on the ultimate size, and phase-in of credits should be referred to the Budget Review Board for recommendation to the President.
- **Policy of Non-Discrimination:** The tax credit is subject to a policy against discrimination.
- **A Limited Federal Presence:** Because the tax credit does not constitute a form of direct Federal financial assistance to institutions, it does not open a window for future intrusive Federal action.

STATEMENT OF THE ISSUE

The right of parents to direct the education of their children is a firmly established policy in American jurisprudence. More than half a century ago, in the landmark case of Pierce v. Society of Sisters, the Supreme Court decided that the Constitution protects parents' choice to have their children educated at private schools rather than in public institutions. However, economic, social, and political changes have occurred since Pierce which, in many instances, have rendered this constitutional protection effectively meaningless.

On the one hand, parents who choose to have their children educated at a non-public school must bear the constantly escalating tuitions which those schools must charge to survive. On the other hand, these same parents must support public education through taxes which are paid by all citizens.

For many parents, this dual financial burden is too great to permit them to exercise the right to send their children to a non-public school of their choice. Therefore, tax relief for non-public school tuition expenses is necessary as an issue of equity if American families are to continue to have a meaningful choice between public and private education at the elementary and secondary level.

BACKGROUND

Constitutionality:

Courts which have confronted state tuition tax credit legislation have displayed the uncertainty which characterizes this issue: five courts have found such legislation to be unconstitutional, whereas two others have found no constitutional deficiencies.

The courts which have invalidated tuition tax benefit programs have done so on the basis of an inability to discern a "secular effect" in the legislation. Therefore it is crucial for the administration to build a case for the secular purposes served by a tuition tax credit bill. The Working Group has inserted specific language in the preamble to the Act which meets this test. (refer to Section 2 in the attached bill).

Refundability:

The Working Group believes that although refundability would provide assistance to needy families who are not now taxpayers, this feature is not desirable. It would be costly to make the credit refundable to families who have no tax liability.

Moreover, refundability of tuition tax credits could set a forceful precedent for the use of the tax system to deliver other types of Federal assistance programs.

OPTIONS

The Working Group recommends introduction of tuition tax credit legislation in the 97th Congress, and a restriction of the tax credit to parents of students in private, non-profit, elementary and secondary schools.

The introduction and enactment of legislation this year meets the President's campaign commitment, and addresses the concerns of those who recall President Carter's reversal of policy regarding support for tuition tax credits.

Limiting the tax credit is recommended in light of changes being made in current Federal programs for post-secondary student financial assistance, and as a way to control program costs. The Treasury has estimated that the extension of tax credits to post-secondary students would approximately triple the revenue impact of the program.

1. RECOMMEND INTRODUCTION OF TUITION TAX CREDIT LEGISLATION IN THE 97TH CONGRESS.

_____ Approve _____ Disapprove

2. RESTRICT CREDITS TO PARENTS WITH CHILDREN IN PRIVATE NON-PROFIT PRIMARY AND SECONDARY SCHOOLS ONLY.

_____ Approve _____ Disapprove

The Treasury Department has provided the following preliminary estimates as a guide to the costs of the proposed tuition tax credit proposal. The estimates are based on the following assumptions: initiation of the program in January of 1983; 5 million initial potential recipients; a 3 year phase-in: \$100 in 1983, \$300 in 1984, \$500 in 1985; and a small estimated first year effect, since most individuals would receive the credit on or before April 15, 1984. However, the Working Group recommends that a final decision on the phase-in and level of credits be made by the Budget Review Board.

A Tuition Tax Credit Equal to 50% of Tuition Payments

(billions)

1982	1983	1984	1985	1987	1988
-	0.1	0.6	1.6	2.5	2.6

Office of the Secretary of the Treasury, March 16, 1982
Division of Tax Analysis

3. REFER LEVEL OF TAX CREDITS AND PHASE-IN TO THE BUDGET REVIEW BOARD.

_____ Approve _____ Disapprove

One way to delay the revenue impacts from a tuition tax credit program is to phase the program in by grade increments. This alternative would extend the phase-in period, but would require a higher initial level of credit in order to be credible. The Working Group believes that this proposal carries a built-in growth dynamic during the legislative process to extend credits to post-secondary schools, and therefore believes it would be more advantageous to initiate a smaller credit which covers all intended beneficiaries from the beginning.

4. RECOMMEND THAT THE TAX CREDIT PROGRAM NOT BE PHASED-IN BY GRADE.

_____ Approve _____ Disapprove

One further way to control costs would be to limit the credit to those under a certain income level. Such targeting would insure that the benefits of the program would be received by those most in need.

The Working Group rejected this option because it converts a tax equity proposal into a program for income redistribution. When a similar initiative was introduced by Senator Metzenbaum in 1978 4 Republicans (Griffin, Hatfield, Javits and Stafford) joined 35 Democrats in voting for the proposal, and 34 Republicans joined 24 Democrats in voting against.

5. SET A RESTRICTION OF THE TAX CREDIT BY INCOME LIMITS.

_____ Approve _____ Disapprove

A bill to amend the Internal Revenue Code of 1954 to provide a Federal income tax credit for tuition.

Be it enacted by the Senate and House of Representatives of the United States of America in Congress assembled.

SEC. 1. SHORT TITLE.

This Act may be cited as the "Educational Opportunity and Equity Act of 1982".

SEC. 2. CONGRESSIONAL FINDINGS.

The Congress finds that it is the policy of the United States to foster educational opportunity, diversity, and choice for all Americans. Therefore Federal legislation should recognize that --

(A) pluralism is one of the great strengths of American society, that diversity in education is an important contributor to that pluralism, and that nonpublic schools play an indispensable role in making that diversity possible;

(B) the existence and availability of alternatives to public education tends to strengthen public education through competition and improves the educational opportunities of all Americans;

(C) Americans should have equal opportunities to choose between the education offered by public schools and that available in private educational systems and should not

be compelled because of economic circumstances to accept education provided by government created and government operated school systems, and that to force such a selection is an unfair and unjust discrimination against persons of lesser means;

(D) increasing numbers of American families are unable to afford nonpublic school tuition in addition to the state and local taxes that go to support public schools, and that tax relief for nonpublic school tuition expenses is necessary if American families are to continue to have a meaningful choice between public and private education at the primary and secondary level;

(E) tax relief in the form of tuition tax credits is the fairest way to extend a choice in education to a wide range of individuals at all income levels, that tax relief in the form of tuition tax credits creates the least possible danger of entanglement between government and the value structures of the various nonpublic school systems and of interference in the lives of individuals and families consistent with achieving these ends, and that tax relief in the form of tuition tax credits achieves these ends with a minimum of complexity so that those for whom the tax relief is intended will be able to understand and take advantage of it;

more educational institutions for himself, his spouse, or any of his dependents (as defined in section 152).

"(b) LIMITATIONS.

"(1) MAXIMUM DOLLAR AMOUNT PER INDIVIDUAL. The amount of the credit allowed under subsection (a) for the taxable year with respect to amounts paid on behalf of each individual for which a credit is claimed shall not exceed--

"(A) \$ in the case of tuition expenses paid during calendar year

"(B) \$ in the case of tuition expenses paid during calendar year

"(C) \$ in the case of tuition expenses paid during calendar year and thereafter.

"(2) SPOUSE. No credit shall be allowed under Subsection (a) for amounts paid during the taxable year for the education of the spouse of the taxpayer unless--

"(A) the taxpayer is entitled to an exemption for his spouse under section 151(b) for the taxable year, or

"(B) the taxpayer files a joint return with his spouse under section 6013 for the taxable year.

"(c) SPECIAL RULES.

"(1) ADJUSTMENT FOR SCHOLARSHIPS AND FINANCIAL ASSISTANCE.

"(A) REDUCTION OF EXPENSES. The amounts otherwise taken into account under subsection (a) as tuition expenses of any individual for any taxable year shall be reduced (before the application of subsection (b)) by any amounts attributable to the payment of educational expenses which were received with respect to such individual for the taxable year as a scholarship, fellowship, or other financial assistance which is exempt from income taxation by any law of the United States (other than a gift, bequest, devise, or inheritance within the meaning of section 102(a)).

"(2) DISALLOWANCE OF CREDITED EXPENSES AS DEDUCTION.

No deduction or credit shall be allowed under any other section of this chapter for any tuition expense to the extent that such expense is taken into account in determining the amount of the credit allowed under subsection (a).

"(d) DEFINITIONS. FOR PURPOSES OF THIS SECTION

"(1) ELIGIBLE EDUCATIONAL INSTITUTION. The term eligible educational institution, means--

"(A) an elementary or secondary school is a privately operated, not-for-profit, day or residential

school which provides, respectively, elementary or secondary education and which--

"(i) is exempt from taxation under section 501(a) as an organization described in section 501(c)(3), and

"(ii) since its designation as an organization exempt from taxation, has not denied admission to any person or excluded any person from participation in any school program, activity or benefit, on account of race, color, or national or ethnic origin.

"(2) TUITION EXPENSES. The term "tuition expenses," means tuition and fees required for the enrollment or attendance of a student at an educational institution, including required fees for courses, and does not include any amount paid for books, supplies, meals, lodging, transportation, or personal living expenses.

"(e) TAX CREDIT NOT TO BE CONSIDERED AS FEDERAL FINANCIAL ASSISTANCE TO INSTITUTION. No educational institution which enrolls a student for whom a tax credit is claimed under the amendments made by this Act shall be considered to be a recipient of federal financial assistance under this Act.

SEC. 4. EFFECTIVE DATE.

The amendments made by section 3 of this Act shall apply to taxable years beginning on January 1, 1977, for amounts paid on or after that date.